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Foreign Activity

AN ANALYSIS OF FOREIGN PARTICIPATION IN U. S. EQUITIES MARKETS
by the SIA Research Department

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FOREIGN ACTIVITY IN U.S. SECURITIES

HIGHLIGHTS

1. Net foreign investment (purchases less sales) in U.S. equities reached only $355 million in the third quarter, a drop of nearly 65% relative to both the second and first quarters. Also, this was the lowest quarterly level since the third quarter of 1979. Only modest purchases were made despite the explosive stock market rally which started in mid-August. Sales exceeded purchases by $170 million in September when total foreign activity soared. Obviously, foreign investors did not believe the stock market rally would be sustained.

   In contrast, U.S. investors thought the stock market rally would continue. For example, net purchases of corporate equities by insurance companies reached $2.0 billion, private pension funds $1.8 billion, and state and local government employee retirement funds $1.4 billion.

2. Foreign gross activity (purchases plus sales) in U.S. equities climbed to $20.2 billion, or more than 50% greater than in either the second or first quarters. This was the highest level since the second quarter of 1981. As indicated, gross activity climbed in September when it exceeded August by 56% and July by 71%.

3. Net purchases of corporate bonds by foreigners amounted to only $56 million compared to nearly $1.3 billion in the second quarter. Almost all net purchases occurred in July. The drop in interest rates during the third quarter made these securities less attractive relative to other investments.

4. Interest in Treasury securities climbed as foreign holdings jumped about $5.2 billion in the third quarter. A flight to quality was the essential reason for this high level of interest in U.S. Government obligations. German and Mideast investors were particularly interested in these securities.

5. U.S. investors' net purchases of foreign stocks amounted to $109 million, almost unchanged from the $99 million in the second quarter. Net purchases occurred only in September largely because of an expected appreciation in foreign stock prices and a strengthening in foreign currencies relative to the dollar. The dollar has since weakened relative to many major currencies. For example, from September to mid-December, the dollar depreciated against the Japanese yen, Swiss franc and German mark, 6.8%, 3.8% and 3.3%, respectively.

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Introduction

The dollar continued to appreciate relative to most foreign currencies during the third quarter. This occurred despite a steep drop in U.S. short-term interest rates as well as a significant narrowing of both short- and long-term interest rate differentials favoring the U.S. dollar. The dollar lost ground against only one foreign currency, the Canadian dollar, as declines in Canadian interest rates lagged those in the U.S.

Overall, the dollar was not adversely affected by the less restrictive Federal Reserve policy because of interest rate and non-interest rate considerations. Foreign central banks used this opportunity to reduce their interest rates in order to stimulate economic activity. Nevertheless, there were still some interest rate advantages to holding dollars. Long-term rate differentials narrowed less than short-term rates. A positive yield curve developed because of significant demand for funds from the government sector and corporate efforts to restructure debt from short to long-term. Concern existed among investors about the long-term consequences of projected U.S. government deficits. In addition, there was fear that interest rate declines would be limited by Federal Reserve monetary policy because money supply growth was at the upper end of their targets.

Non-interest rate factors also supported the dollar. Safety considerations contributed to the dollar's strength. Economic, political and military insecurities increased in the world. Foreign investors viewed the long-term economic prospects of the U.S. optimistically. However, the U.S. current account balance deteriorated in the third quarter and posted a deficit for the first time since the fourth quarter of 1981.

U.S. economic activity continued at a low level during the third quarter as real GNP rose only slightly despite an easing of monetary policy. Weakness was again evident in interest-rate sensitive components. Final sales (all GNP components except inventories) fell because of decreases in fixed investment and consumer purchases of durable goods. Net exports declined because of the strong dollar. Business inventories rose due to weak sales. Nevertheless, there were some positive economic signs. After-tax profits for U.S. corporations rose modestly. Also, inflation continued to remain at a low rate. The GNP implicit price deflator was 4.7 percent in the third quarter. Just one year ago, this inflation rate was 9.9%.

Other industrialized countries continue to experience either recession or very sluggish economic growth. High real interest rates and depressed world trade are affecting the economies of these countries. Canada's GNP fell in the third quarter for the fifth consecutive quarter. Most European countries remain in recession. West Germany's economy is stagnating partly because

of its dependency on slow-growth heavy industry and adverse fiscal policies. Unemployment rose and is reaching post-World War II record levels. Britain's industrial production again fell reaching its lowest quarterly level in 15 years. The Japanese economy is growing but relatively slowly because of depressed world trade and sluggish domestic demand. As a result, their unemployment rate is also reaching an historically high level. The most encouraging event during the third quarter for the industrialized countries was the drop in U.S. interest rates, thereby taking pressure off their exchange rates. A decline in U.S. rates allows foreign countries to lower their interest rates and might eventually result in stimulating their domestic economies.

In the third quarter, the dollar appreciated against all major currencies except the Canadian dollar. The dollar gained sharply against the Japanese yen, 4.5%, and French franc, 4.1%. More modest dollar appreciation occurred relative to the Swiss franc, German mark, and British pound, 2.8%, 2.5%, and 2.3%, respectively.

Stock price indexes climbed in the third quarter because of significant increases in August and September. The NYSE stock price index rose 9.8%, while the AMEX index jumped 12.9% and the DJI average increased 10.4%. In addition, the NYSE experienced record highs of average daily share volume in August (76.0 million) as well as the dollar value of shares traded in August ($46.2 billion) and September ($46.8 billion). Theoretically, the strong U.S. stock market was expected to attract significant foreign funds.

Foreign Investments in U.S. Equities

Gross Activity

Foreign gross activity (purchases plus sales) in U.S. equities climbed to $20.2 billion, the highest level since the second quarter of 1981. Overall, third quarter gross activity rose about 50% relative to the low levels in each of the first two quarters of 1982. Foreign interest in U.S. equities was stimulated by significant increases in the stock market resulting from the less restrictive Federal Reserve policy. Gross activity rose somewhat during July and August, but soared in September. The proportion of regional activity shifted during the third quarter, although the absolute levels significantly increased for each region. Latin America's proportion of total activity increased most significantly to 11% from 9.3% in the second quarter. Canada's share of the total also rose while both Asia's and Europe's shares fell.

Net Purchases

Third quarter net purchases by foreign investors of U.S. equities fell to a surprisingly modest $355 million, a drop of nearly 65% relative to both the second and first quarters.

This was the lowest quarterly level since the third quarter of 1979. The diminished interest in U.S. equities took place despite the significant drop in U.S. interest rates and resulting explosive stock market rally. Net purchases were made only during August and in September net sales actually resulted. Although the stock market rally began in August, foreign investors apparently were not convinced that the market's rally was sustainable and net sales of $170 million were made in September.

TABLE I

GROSS TRANSACTIONS IN AND NET PURCHASES OF U.S. EQUITIES
($ Millions)

	1982 Second Quarter		1982 Third Quarter	
	Gross	Net	Gross	Net
Europe	$ 7,783	$611	$11,436	$290
Belgium-Luxembourg	269	5	368	(8)
France	962	(40)	1,045	(51)
Germany	523	81	785	(39)
Netherlands	384	50	508	(46)
Switzerland	2,050	(144)	3,395	(225)
United Kingdom	3,253	667	4,896	732
Canada	1,736	(8)	2,674	146
Latin America	1,237	101	2,240	(102)
Bermuda	440	28	723	15
Netherlands Antilles	204	14	692	(46)
Asia	2,483	217	3,716	(6)
Hong Kong	314	14	439	39
Japan	314	(100)	515	(153)
"Other Asia"*	1,734	238	2,684	104
All Countries	$13,311	$975	$20,195	$355

Source: U.S. Treasury

* Countries included are: Bahrain, Iran, Iraq, Kuwait, Oman, Saudi Arabia, the United Arab Emirates.

European Investors

Net purchases by European investors plunged to $290 million in the third quarter. This was more than 50% below the second quarter's level of $611 million. All major European countries

except Britain were net sellers. Net purchases were made in July and August. However, in September net sales of $266 million occurred because of portfolio adjustments, profit taking and expected changes in foreign exchange rates.

British investors' net purchases rose in the third quarter to $732 million, about 10% above the second quarter's level of $667 million. Most of the net purchases occurred in July ($297 million) and August ($363 million) when British investors accelerated their buying activities. However, in September net purchases plunged to only $72 million. The higher level of British purchases in July and August resulted from the anticipated depreciation of the pound. The present current account surplus on the balance of payments is expected to be eliminated in 1983. Imports are forecasted to rise substantially because consumer spending has recently started to soar. Also, oil prices could continue to fall because of slack world demand. The drop in net purchases in September can be attributed to significant portfolio adjustments as evident by the jump in gross activity.

Swiss investors continued to sell U.S. equities for the fifth consecutive quarter. Net sales in the third quarter accelerated to $225 million or 56% greater than in the second quarter. This was the largest Swiss divestiture of U.S. equities since the third quarter of 1980. Most net sales occurred in September when gross activity soared. The large volume of selling took place largely because it was believed that the U.S. stock market rally was probably not sustainable. Also, Swiss equities and the Swiss franc are looking more attractive. Appreciation in Swiss stock prices is anticipated because of falling interest rates and modest economic growth beginning later in 1983.

German investors were net sellers of $39 million of U.S. equities in the third quarter. In the second quarter, net purchases of $81 million were made. Net sales last occurred in the fourth quarter of 1981. The significant rise in U.S. equity prices along with some positive domestic economic factors encouraged a small percentage of German investors to realize profits. The German economy is stagnating and the outlook is not optimistic. However, the mark has been strong against the currencies of most of its important trading partners and is expected to remain so. The German current account will be in balance this year partly because of reduced outflows for services while the recession has depressed imports. Inflation has fallen below 5% and can be expected to decline as trade union wage settlements have been below the inflation rate. Real interest rates are still high even though the Bundesbank eased monetary policy in August. The Centre-Right government, before taking office, announced its intentions to reduce government expenditures and cut borrowing.

Canadian Investors

Canadian investors were net purchasers of $146 million of U.S. equities in the third quarter compared to net sales of $8 million in the second quarter. This is the first time they have been net

purchasers since the third quarter of 1981. The possibility of future weakening of the Canadian dollar relative to the U.S. dollar helps to explain the behavior of Canadian investors. The Canadian government did not permit interest rates to fall as fast as in the U.S. during the third quarter in order to help control inflation and to strengthen their currency. As a result, Canadian interest rates at the end of the third quarter were significantly higher than those in the U.S., and Canada's economy remains mired in a deep recession.

Asian Investors

Asian investors in the third quarter were net sellers of U.S. equities for the first time since the second quarter of 1980. However, net sales amounted to only $6 million, with a large proportion of sales occurring in July. This occurred because of large Japanese net sales and diminished interest by the oil-exporting countries. Japanese investors were again net sellers throughout this quarter. Their net sales amounted to $153 million compared to $100 million in the second quarter. Expectations increased that the yen would appreciate because of future higher Japanese trade surpluses as well as more favorable capital flows. Also, the yen could be expected to appreciate because of the need to relieve trade disagreements with the U.S. and Japan's other principal trading partners. In addition, Japan's basic balance (current account plus long-term capital account) achieved a $1 billion surplus in September; the first such surplus in nearly a year. In contrast, Mideast investors continued to buy U.S. equities although their net purchases dropped 56% to $104 million from $238 million in the second quarter. The third quarter level was the lowest since the first quarter of 1981. Net sales occurred in July apparently because the trade-weighted value of the dollar declined during the latter half of this month. However, oil-exporting nations did not believe the dollar would depreciate or stock market rally end since net purchases were made in August and September.

Latin American Investors

In Latin America, net sales of $102 million were made while in the second quarter there were net purchases of $101 million. Most net sales occurred in Netherlands Antilles ($46 million), British West Indies ($19 million), and Mexico ($18 million). Here also, most net sales took place in September. There was a lack of conviction that the stock market rally would persist as well as expectations that the dollar would weaken.

Foreign Investment in U.S. Corporate Bonds

Foreign investment in U.S. corporate bonds amounted to only $56 million in the third quarter; the smallest total since the third quarter of 1979. Net purchases in the second quarter were nearly $1.3 billion, the second highest quarterly figure since

the first quarter of 1981. The drop in net purchases correlates with the decline in yields throughout the third quarter. Yields on long-term corporate bonds declined relatively moderately in July, dropped substantially in August and continued falling in September. Net purchases of corporate bonds amounted to $181 million in July, plunged to $5 million in August, and net sales of $130 million occurred in September. Obviously, the lower yields on U.S. corporate bonds dampened foreign interest in these investments.

Net purchases in U.S. corporate bonds in the third quarter resulted from continued German interest. German investors made net purchases of $451 million; the second highest quarterly figure. The most significant increase, $899 million, occurred in the previous quarter. Apparently, these investments are being made because the U.S. is viewed as a "safe haven" rather than for return on investment considerations. Net sales were made by other European countries. British investors' net sales of $169 million were one of their largest quarterly divestitures of U.S. corporate bonds. Most of these sales occurred in September when the differential between U.S. and British corporate bond yields narrowed considerably. Oil-exporting countries continued to be net sellers in the third quarter.

Interest rate differentials between the U.S. and other major industrial countries narrowed in the third quarter, as shown in Morgan Guaranty's "World Financial Markets." The U.S. long-term corporate bonds yield dropped 287 basis points while those in the U.K. fell 211 basis points. German yields did not change while Swiss yields actually rose slightly.

TABLE II

GROSS ACTIVITY AND NET PURCHASES OF U.S. CORPORATE BONDS
($ Millions)

	1982 Second Quarter		1982 Third Quarter	
	Gross	Net Purchases	Gross	Net Purchases
Europe	$3,485	$1,243	$3,717	$259
Belgium-Luxembourg	59	(3)	109	(31)
Germany	1,191	899	1,393	451
Switzerland	333	107	335	(17)
United Kingdom	1,253	115	1,465	(169)
"Other Asia"	419	(169)	554	(102)
Total	$4,986	$1,274	$5,676	$ 56

Source: U.S. Treasury

Foreign Investment in U.S. Treasury Notes and Bonds

Foreign investment in U.S. Treasury notes and bonds climbed by nearly $5.2 billion in the third quarter, one of the largest quarterly increases. Net purchases of Treasuries rose $2.8 billion in the second quarter and $5.4 billion during the first quarter. The significant third-quarter level is largely attributable to the $4.3 billion jump in European net purchases. German holdings climbed $2.7 billion while British rose $672 million. Oil-exporting countries continued their large investments in Treasuries with net purchases of $1.8 billion.

The flight to quality is the essential reason for the significant level of foreign purchases of Treasuries. This buying is not surprising considering the obvious strains on the international financial system because of potential defaults. In addition, other economic as well as political and military insecurities exist. The significant third quarter rise in German holdings of Treasuries is also attributable to the flight to safety. German investors appear to be concerned about the domestic economy's continuing recession and the jump in corporate bankruptcies. Large German banks have significant exposure to loans made to countries in the Eastern bloc as well as Latin America. Additional uncertainties were created because of the perspective change in government.

TABLE III

NET FOREIGN PURCHASES AND TOTAL FOREIGN HOLDINGS OF U.S. TREASURY NOTES AND BONDS

($ Millions)

	1982 Second Quarter		1982 Third Quarter	
	Net Purch.	Estimated Holdings[1]/	Net Purch.	Estimated Holdings[1]/
Europe	$ 94	$21,939	$4,290	$26,229
Switzerland	13	588	195	783
West Germany	418	9,850	2,738	12,588
United Kingdom	(373)	6,664	672	7,336
Asia	2,973	45,640	2,227	47,867
Japan	(67)	11,136	258	11,394
"Other Asia"	2,737	32,891	1,796	34,687
All Countries	$2,825	$74,523	$5,169	$79,692

Source: U.S. Treasury

1/ Treasury has discontinued publication of the estimated foreign holdings of marketable Treasury notes and bonds. Therefore, estimated holdings are based on SIA's summation of reported monthly flows.

U.S. Investor Activity in Foreign Stocks

In the third quarter, U.S. investors' net purchases of foreign securities inched up to $109 million from $99 million in the second quarter. Net purchases occurred only in September as net sales took place in both July and August. This pattern is partially explained because in September it appeared more probable that the prices of certain foreign stocks would rise. Also, market expectations became more widespread that some foreign currencies would appreciate relative to the dollar. In fact, the dollar has since weakened against many major currencies. For example, from September to mid-December, the dollar depreciated against the Swiss franc, German mark, and Dutch guilder, 3.8%, 3.3% and 2.5%, respectively.

A large proportion of U.S. investment activity occurred in European stocks where net purchases amounted to $129 million compared to $55 million during the second quarter. The third quarter rise was the highest this year. A large proportion of net purchases were reportedly made in French stocks. This represented a significant change from previous U.S. investors' behavior. Throughout 1982, net sales had occurred in French stocks. It is difficult to understand these purchases of French stocks. A statistical error might have been made. The economy is in serious trouble and the outlook is not encouraging. French economic growth is being slowed to help reduce the high inflation rate. GNP fell 0.9% in the third quarter. The only encouraging news is the resulting decrease in imports. Still, a current account deficit will exist in 1982 which will put pressure on the franc. In contrast, U.S. investor net purchases of both Dutch and Swiss stocks declined compared to the second quarter. Third quarter net purchases of Dutch and Swiss stocks amounted to $13 million and $14 million, respectively. Net sales again occurred in British stocks but the amount was a modest $4 million. U.S. investors have made divestitures of British stocks throughout 1982.

Modest net sales of $12 million occurred in Asian stocks. However, net purchases of $21 million were made in Japanese stocks, determined only by activity in September. Apparently, U.S. investors expect the yen to appreciate relative to the dollar. Also, Japanese economic growth is expected to modestly rise in 1983 because of some improvement in world trade. This forecast regarding the strength of the yen has so far been correct. From September to mid-December, the yen appreciated 6.8% relative to the dollar.

U.S. investors divested themselves of Canadian stocks. Net sales were $66 million in the third quarter compared to net purchases of $34 million in the second quarter. The value of the Canadian dollar is expected to fall relative to the U.S. dollar because it is believed that Canadian interest rates will be lowered to enable its economy to escape from the current recession.

TABLE IV

GROSS ACTIVITY IN AND NET PURCHASES OF FOREIGN STOCKS BY U.S. INVESTORS
($ Millions)

	1982 Second Quarter		1982 Third Quarter	
	Gross	Net Purchases	Gross	Net Purchases
Europe	$1,167	$ 55	$1,475	$129
France	146	(6)	141	51
Netherlands	65	19	71	13
Switzerland	130	26	148	14
United Kingdom	626	(10)	880	(4)
Canada	504	34	678	(66)
Asia	1,212	2	768	(12)
Japan	1,043	(9)	613	21
Other	188	8	232	58
All Countries	$3,071	$ 99	$3,153	$109

Source: U.S. Treasury

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NOTE

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FOREIGN ACTIVITY IN U.S. SECURITIES

"HIGHLIGHTS"

1. As evidenced by the moderate level of foreign portfolio investment in 1982, the strength of the dollar is not the sole consideration for investment in U.S. securities. Given a languishing economy, intense political debate over monetary and fiscal policy, and a lackluster stock market over much of the year, foreign net purchases of U.S. equities dropped 34% from 1981's record of $5.8 billion to $3.9 billion in 1982.

2. Foreign investors were slow to catch the market rally, but net purchases of equities spurted in December to $915 million, close to the pace of the entire first or second quarter. In the last quarter, foreign net purchases reached the quarterly high for the year, $1.5 billion

3. Overall, German investors showed an unusual enthusiasm for U.S. securities. Despite a past aversion to equity investment, German investors purchased over $300 million of U.S. equities in 1982. Moreover, large net purchases, $1.9 billion, were made of corporate bonds and an unprecedented $5.3 billion of U.S. Treasuries.

4. In contrast, given oil price uncertainty and dwindling surpluses, the oil-exporting countries cut down on investment in U.S. securities. Moderate purchases of $376 million of equities were made in 1982, in contrast to $1.2 billion in 1981. In addition, although still substantial, net purchases of U.S. Treasuries, a traditional favorite investment vehicle of these countries, dropped from $11.2 billion in 1981 to $7.5 billion in 1982. All told, foreign holdings of U.S. Treasuries increased 26%, or $17.3 billion, to an estimated $83.5 billion.

5. With the exception of the second quarter when U.S. interest rates spurted, foreign investors showed little enthusiasm for U.S. corporate bonds. Foreign net purchases of corporate bonds slid from $3.5 billion in 1981 to $1.5 billion in 1982.

6. U.S. investors showed minimal interest in foreign securities in the first three quarters of 1982 but, in the fourth quarter, U.S. interest revived to the tune of $1.3 billion in net purchases. Based on fourth quarter activity, U.S. net purchases of foreign securities in 1982 totaled $1.3 billion, impressively up from $188 million in 1981.

Introduction

In a virtual repeat performance of 1981, the dollar advanced against most major currencies in 1982. The relative strength or weakness of the dollar is a prime consideration for foreign investment in U.S. equities. However, as evidenced by the comparably moderate level of foreign investment in 1982, the dollar is not the sole consideration. Given an uncertain economic climate, heated political debate over monetary and fiscal policy, and a lackluster stock market during the first seven months, foreign investment in U.S. equities dropped 34% from 1981's record of $5.8 billion to $3.9 billion in 1982.

In the first quarter of the year, the U.S. economic outlook remained glum and the stock market reflected the depressed picture. However, the dollar advanced buoyed by rising interest rates and a favorable current account position. On the other hand, foreign countries showed minimal signs of recovery and the level of U.S. interest rates limited the policy options of foreign governments. Foreign investors escalated net purchases of U.S. equities to $977 million from a low $443 million in the fourth quarter of 1981.

The second quarter of 1982 brought mixed economic news. Projected budget deficits grew larger, fed by high interest rates and a languishing economy. While U.S. unemployment soared to a 40-year high, consumer prices dropped a surprisingly large 0.3% in March but spurted 1% in May. A distinct bright spot--the index of leading indicators registered its first significant gain of the the year in April. The Falklands crises dominated international news, adding to an increasingly strained political and economic international scene. With the dollar remaining strong, net foreign investment in U.S. equities was sustained at the first quarter's level, $975 million.

In the third quarter, the dollar continued to appreciate relative to most foreign currencies although not with the strength evidenced during the first half of the year. The Federal Reserve adopted a less restrictive monetary policy and interest rates trended down. Prompted in part by declining rates, the stock market began an explosive, though erratic, rally. Foreign countries grasped the opportunity to allow their interest rates to ease in the hopes of stimulating economic recovery. However, foreign interest in U.S. equities took a surprising plunge, dropping 64% to $355 million. Apparently, the foreign investor was betting on a weaker dollar and a short-lived market rally.

The fourth quarter confirmed the durability of the stock market rally, with the Dow Jones Industrial Average crossing the 1000 level for the first time in more than 15 months in October. While the stock market continued its rise, slow progress was made toward economic recovery. Inflation seemed well under control, but real GNP contracted at a 1.9% annual rate and unemployment hit double-digit numbers. Foreign investors were slow to catch

the market's rally, but net purchases in December at $915 million were close to the pace of the entire first or second quarter. Foreign net purchases in the fourth quarter reached 1982's quarterly high, $1.5 billion.

Exchange Rates

Similar to 1981, the dollar enjoyed a robust year in 1982, rising against all major currencies. From year-end 1981 to year-end 1982, the dollar gained almost 16% against the British pound and the French franc. The Swiss franc suffered an 11% depreciation against the dollar, while the mark and yen gave up around 6%. The Canadian dollar's loss of 4% was modest in comparison.

Repeating the pattern of 1981, the dollar's position generally deteriorated in the fourth quarter. From end-September to end-December, the yen appreciated a sharp 15% against the dollar. Other major currencies had gains ranging from 8% for the Swiss franc to less than 1% for the Canadian dollar. Only the British pound failed to advance against the dollar and continued its year-long depreciation.

Stock Market Indices

During 1982, the stock market fell consecutively from January through March, regained ground briefly in April, then declined to bottom out in July. The market rally, which began in August, pushed the stock indices to impressive year-end closings. From December 1981 to December 1982, the NYSE stock price index climbed 14%; the DJI Average, 20%; and the S&P 500 index, 15%. Much of the market's steam came in the late third and fourth quarters. However, despite a significantly improving stock market in the fourth quarter, foreigners were cautious investors.

Foreign Activity in U.S. Equities

Gross Activity

Although net purchases of U.S. equities by foreign investors dropped off sharply in 1982, gross activity inched up 6% to $80.1 billion from $75.5 billion in 1981. The increased activity of European and Asian investors offset the 12% decrease in activity by Canadian investors. Gross activity by Asian investors rose 16% to $14.9 billion, while European investors accelerated activity by 9% to $46.8 billion. By and large, the bulk of the rise in European activity stemmed from British investors, who upped transactions by 40% to $18.8 billion from $13.4 billion in 1981.

TABLE I

GROSS TRANSACTIONS IN AND NET PURCHASES OF U.S. EQUITIES
($ Millions)

	1981		1982	
	Gross	Net	Gross	Net
Europe	$42,922	$3,662	$46,798	$2,530
Belgium-Luxembourg	1,625	119	1,583	(81)
France	5,508	900	5,019	(147)
Germany	3,877	(23)	3,367	321
Netherlands	2,154	42	2,095	(55)
Switzerland	14,866	288	14,162	(524)
United Kingdom	13,427	2,235	18,789	3,041
Canada	11,500	782	10,056	226
Latin America	7,708	(30)	7,672	232
Bermuda	3,037	29	2,715	133
Netherlands Antille	2,150	(98)	1,965	37
Asia	12,935	1,427	14,948	642
Hong Kong	1,392	156	1,734	100
Japan	1,442	118	1,954	1
"Other Asia"*	9,673	1,153	10,668	376
Total All Countries	$75,542	$5,830	$80,084	$3,850

Source: U.S. Treasury

* Countries included are: Bahrain, Iran, Iraq, Kuwait, Oman, Saudi Arabia, the United Arab Emirates.

Note: All 1981 figures reflect Treasury revisions as of first quarter 1983. All 1982 figures are based on Treasury preliminary quarterly numbers.

Net Purchases

Foreign net purchases of U.S. equities sank 34% in 1982 to $3.9 billion from 1981's record $5.8 billion. While 1982's foreign investment is disappointing by 1980 and 1981 standards, it still represents one of the highest levels reached in the 1972-82 period. The over $5 billion in foreign funds invested in U.S. equities in 1980 and 1981 topped the $4.7 billion record of 1975. However, investment in the years between records ranged from a high of only $2.8 billion and a low of $540 million.

On a regional basis, 1982 activity resulted from substantially reduced net purchases by three of the four major regions. Canadian investors cut back net purchases by 70% from the 1981 level; Asian investors, by 55%; and European investors, by 31%. Given considerable turmoil in Latin America, it is not surprising that investors from these countries swung from net sellers of $30 million in 1981 to net purchasers of $232 million in 1982.

European Investors

Net purchases by European investors fell 31% in 1982 to $2.5 billion from 1981's $3.7 billion. In a distinct departure from the prior year's pattern when only one major country, Germany, was a net seller, four countries were net sellers in 1982. As has been the case in recent years, British investors were the mainstay of European investment, boosting net purchases 36% from the 1981 level. Also offsetting net selling was the turnaround by German investors to net purchasers of over $300 million, a substantial amount for these investors.

British Investors

Major progress has been made in controlling inflation in the U.K., around a 6% annual rate for 1982, but prospects for economic recovery are still dim. Real GNP advanced at a 0.5% annual rate, after declining in the two previous years accompanied by skyrocketing unemployment. The pound reflected the woes of the economy over the year, particularly in the fourth quarter when every other major currency appreciated vis-a-vis the dollar. Contributing to the end of the year slide was a short-lived moderation in U.K. interest rates, the expected oil price drop, and speculation over early national elections.1/ The possibility of a victory by the Labour Party with its stated commitment to a 30% devaluation of the pound over a two year period left investors reluctant to hold long positions in sterling. The coincidental rally in the U.S. stock market and upsurge of pressure on the pound prompted a 28% increase in British investment in equities from the third quarter's $732

1/ Economic Week, Citibank, 1/24/83.

million to $938 million in the fourth quarter. The last quarter pickup pushed British investment in U.S. securities in 1982 to $3.0 billion, almost 36% above the 1982 level of $2.2 billion.

German Investors

Similar to British investors, German investors showed a distinct enthusiasm for U.S. equities in the fourth quarter, with net purchases of $211 million made. Net purchases for 1982 totaled $321 million, an atypically high level for German investors who were net sellers of $23 million in 1981. Moreover, German investors evidenced considerable interest in U.S. corporate bonds and Treasuries in 1982. The German economy was beset by lingering recessionary problems in 1982 and the strains on the international banking system aggravated the economic picture. Public concern over the state of the economy was one of the chief factors precipitating the change in governing coalitions in October. In recent years, Germany has experienced heavy capital outflows for overseas investment, a situation which not only adds to current account problems but undermines the revitalization of German industry. While these investment outflows slackened in 1982, investments in the U.S. are still being sought because of the large market and positive business climate with fewer restrictions on profit opportunity.2/

Swiss Investors

Activity in U.S. equities by Swiss investors has historically resulted in annual net sales. However, Swiss investors made net purchases of about $300 million in both 1980 and 1981. In 1982, the Swiss not only adopted their traditional approach to U.S. equities but increased the magnitude of net selling significantly. Net sales were made in every quarter of the year, cumulating in large sales of $524 million. Net selling by Swiss investors escalated in the second half of the year, as the Swiss franc began to recover against the dollar. Prospects of lower inflation, a narrowing interest rate disadvantage, tight control over federal finance and political stability also made Swiss-denominated assets more attractive to hold. However, the Swiss economy is not expected to rebound strongly in 1983 and recovery could be further hampered if political and economic uncertainties in other European countries cause the franc to rise. As the Swiss are intermediaries for the oil-exporting countries, the net selling of U.S. equities may also reflect the recent problems of these investors.

2/ World Financial Markets, Morgan Guaranty Trust Co., 11/82

TABLE II

NET PURCHASES OF U.S. EQUITIES
($ Millions)

	1982 First Quarter	1982 Second Quarter	1982 Third Quarter	1982 Fourth Quarter
Europe	$769	$611	$290	$ 860
Belgium-Luxembourg	(33)	5	(8)	(45)
France	(60)	(40)	(51)	4
Germany	68	81	(39)	211
Netherlands	42	50	(46)	(101)
Switzerland	(54)	(144)	(225)	(101)
United Kingdom	704	667	732	938
Canada	(143)	(8)	146	231
Latin America	(2)	101	(102)	235
Bermuda	22	28	15	68
Netherlands Antilles	(30)	14	(46)	99
Asia	329	217	(6)	102
Hong Kong	40	14	39	7
Japan	(2)	(100)	(153)	256
"Other Asia"	275	238	104	(241)
Total All Countries	$977	$975	$355	$1,543

Source: U.S. Treasury

French Investors

Investment in U.S. equities by French investors shot to a record $900 million in 1981, based mainly on activity in the months surrounding the national elections. However, French investors shunned U.S. equities in 1982, making net sales of $147 million. The stimulative policies of Mitterrand only exacerbated France's economic position leading to large amounts of imports, rising inflation and a huge balance-of-payments deficit. The French government is now "atoning" for these policies with wage and price controls and restrictive monetary and fiscal policies.3/ Nevertheless, the French franc followed a turbulent downward course over 1982 and was devalued some 10% in June. With interest rates on money market instruments the

3/ "Recovery At Last", Business Week, 2/14/83

highest of the major countries in 1982, French investors may have sought these returns rather than investment in foreign equities.

Canadian Investors

Canada's real GNP took a sharp 5% plunge in 1982, while inflation and unemployment remained stuck in double-digit ranges. However, in the latter half of the year, some positive signs emerged. Canadian interest rates followed declining U.S. rates with no adverse effect on the Canadian dollar which, in fact, appreciated vis-a-vis the U.S. dollar over the period. In addition, Canada reported a current account surplus in 1982, the first time in several years. Nevertheless, the strength of a recovery in Canada is predicated on U.S. economic growth. With declining interest rates on domestic money market instruments and a very tenuous recovery, Canadian investors became net purchasers of U.S. equities in the third quarter of 1982 for the first time in a year. Given tne continued boom of the market, Canadian investors upped net purchases by 58% in the fourth quarter to $231 million. However, the revival of interest in U.S. equities was not enough to bring total net purchses for 1982 even close to 1981's $782 million. At $226 million for 1982, net purchases by Canadian investor's were down 71% from the 1981 level.

Latin American Investors

Latin American investors have shown relatively moderate interest in U.S. equities in recent years. In 1981 and 1982, record years for foreign investment in U.S. equities, Latin American investors made net purchases of $148 million and net sales of $30 million, respectively. However, in 1982, Latin American countries experienced serious difficulties in meeting external interest and debt payments and the pace of international lending has consequently slowed. Given extraordinary inflation rates and overvalued currencies, the scaling back of international loans to developing countries will require major policy adjustments by these countries to maintain economic growth. The stability of the dollar and the "safe haven" concept of the U.S. prompted Latin American investors to make net purchases of $232 million of U.S. equities in 1982, with the bulk of these purchases made in the fourth quarter.

Asian Investors

Net purchases of U.S. equities by Asian investors, mainly the oil-exporting countries, have been at exceptional levels in the past two years. However, net purchases in 1982 fell sharply to $642 million from 1981's record $1.4 billion. Net purchases were down materially for Japanese investors, whose net sales during the first three quarters of the year offset net purchases of $256 million in the fourth quarter to produce net purchases of $1 million in 1982. The oil-exporting countries dramatically scaled back net purchases from $1.2 billion to $376 million in 1982. Worldwide progress at reducing oil consumption has translated into lessened demand and falling prices. As equity

investment came into vogue with investors from the oil-exporting countries in the past two years, it is not surprising that, given a lackluster U.S. stock market and prospects for reduced surpluses, these countries were limited buyers of U.S. equities in 1982.

Foreign Investment in U.S. Corporate Bonds

With the exception of the second quarter, foreign investors showed little enthusiasm for U.S. corporte bonds in 1982. Declining interest accelerated from third-quarter net purchases of only $58 million to fourth-quarter net sales of $176 million. All told, foreign net purchases of corporate bonds slid from $3.5 billion in 1981 to $1.5 billion in 1982. On the other hand, gross activity jumped 79% to $21.2 billion from $11.9 billion. The increased activity stemmed from the European countries, with German and U.K. investors about 2 and 4 times as active as in 1981.

In 1982, net purchases of corporate bonds by European investors increased 38% to $2.1 billion from $1.5 billion in 1981. German investors were the main force behind the level of net investment, with net purchases jumping from $740 million in 1981 to $1.9 billion in 1982. Purchases by European investors, however, were offset by net sales of $606 million by the oil-exporting countries. In contrast, investors from these countries were avid purchasers of U.S. corporate bonds in recent years, accounting for $2.0 billion and $1.7 billion of net purchases in 1980 and 1981, respectively. It is not surprising that the oil-exporting countries showed diminished interest in corporate bonds, as their investment in equities and U.S. Treasuries was also reduced in 1982.

Foreign interest in U.S. corporate bonds waxes and wanes mainly on interest rate differentials. From year-end 1981, the average return on U.S. corporate bonds drifted down from 15.50% to 11.75%.4/ However, the spurt in U.S. interest rates in the second quarter attracted $1.3 billion in foreign investment, the quarterly high in 1982. While German corporate bond rates declined some 230 basis points over the year and U.S. rates about 375 basis points, U.S. returns were still considerably above those available on German bonds at the end of the year. In contrast, returns available on U.K. bonds outpaced those of the U.S. during much of 1982 and there was almost constant speculation that U.K. rates would be raised to protect the depreciating pound. U.K. investors made net sales of $273 million of U.S. corporate bonds in 1982, compared with net purchases of $529 million in 1981.

4/ Based on data in World Financial Markets, Morgan Guaranty Trust Co.

TABLE III

GROSS TRANSACTIONS IN AND NET PURCHASES OF
U.S. CORPORATE BONDS
($ Millions)

	1981		1982	
	Gross	Net	Gross	Net
Europe	$ 5,869	$1,499	$13,947	$2,065
Belgium-Luxembourg	242	(42)	362	(112)
Germany	1,478	740	4,612	1,884
Switzerland	802	102	1,356	200
United Kingdom	2,659	529	5,549	(273)
"Other Asia"	3,633	1,657	2,356	(606)
All Countries	$11,862	$3,486	$21,181	$1,529

Source: U.S. Treasury

Foreign Activity in U.S. Treasury Notes & Bonds

Traditionally, foreign transactions in U.S. Treasuries reflect the intervention of central banks in foreign exchange markets to steady their currency vis-a-vis the dollar. As of March 1981, the U.S. announced a policy of limited intervention in currency markets. While foreign central banks have

TABLE IV

NET FOREIGN PURCHASES AND TOTAL FOREIGN HOLDINGS
OF U.S. TREASURY NOTES AND BONDS
($ Millions)

	1981		1982	
	Net Purch.	Estimated Holdings[1]/	Net Purch.	Estimated Holdings[1]/
Europe	$ 1,863	$19,894	$ 7,597	$27,491
Switzerland	105	387	693	1,080
West Germany	1,146	8,238	5,326	13,564
United Kingdom	(614)	6,709	(155)	6,554
Asia	12,559	38,806	10,850	49,656
Japan	1,301	10,780	787	11,567
"Other Asia"	11,156	27,292	7,537	34,829
All Countries	$15,007	$66,261	$17,252	$83,513

Source: U.S. Treasury

1/ Treasury has discontinued publication of the estimated foreign holdings of marketable Treasury notes and bonds. Therefore, estimated holdings are based on SIA's summation of reported monthly flows.

been active in exchange markets to support their currencies, the degree of activity may have been lessened following U.S. policy. This may account partially for the investment pattern that has emerged in recent years. Whereas it could be expected that most major foreign countries would be net sellers of Treasuries given the pressures generated by the rising dollar, this is not the case. Foreign net purchases of Treasuries in 1981 and 1982 show an unprecedented enthusiasm for this investment vehicle. The riskless and liquid market for Treasuries has apparently been attracting considerable attention from foreign investors, thus offsetting central bank intervention. While foreign investors showed scant interest in U.S. corporate bonds, they were avid purchasers of Treasuries. This is consistent with the "flight to quality" theme that prevailed in investment decisions in 1982. Foreign holdings of Treasuries climbed 26%, or $17.3 billion, in 1982 to an estimated $83.5 billion.

European investors made net purchases of $7.6 billion of Treasuries in 1982, compared with $1.9 billion in 1981. The

lion's share of these purchases stemmed from Germany, where net purchases escalated from $1.1 billion in 1981 to $5.3 billion in 1982. The exposure of the German banking system to loan defaults from Eastern block countries and South America coupled with a recessionary climate and a major political upheaval may have prompted German investors to turn to U.S. markets. On the other hand, activity by the U.K. resulted in net sales of $155 million in 1982.

Although still substantial, Asian countries reduced the pace of net purchases of Treasuries by 14% to $10.9 billion in 1982 from $12.6 billion in 1981. The bulk of Asian transactions in Treasuries reflects the activity of the oil-exporting countries. In 1982, these investors cut back net purchases by 32% to $7.5 billion from $11.2 billion in 1981. Declining oil revenues and dwindling surpluses translate into less flexibility and less funds available for external investment. The uncertainty of the oil market situation in 1982 called for shorter-term, liquid investments,5/ prerequisites fulfilled by the U.S. Treasury market. Net purchases originating in Japan also slacken off in 1982, dropping 40% to $787 million from $1.3 billion in 1981.

U.S. Investment in Foreign Securities

Overall, the foreign investment picture in 1982 held little to attract U.S. investors. The economic recovery of the major foreign countries looked less than promising, major national elections carried the risk of dramatic policy changes, the international banking system was unsteady, and currency markets were subject to wide swings. Thus, U.S. investors showed minimal interest in foreign equities through the first three quarters of the year. However, in the fourth quarter, U.S. interest in foreign securities revived to the tune of $1.3 billion in net purchases. Fourth quarter net purchases could have been prompted by a pick up in the stock markets of most foreign countries and the strengthening of many currencies vis-a-vis the dollar. Net purchases of foreign securities in 1982 totaled $1.3 billion, as activity in the first three quarters of the year resulted in a wash. In comparison, U.S. investors purchased only $188 million of foreign securities in 1981 but a record $2.1 billion in 1980. Gross activity declined 17% in 1982 to $15.5 billion from $18.8 billion in 1981.

5/ "The Shrinking Petrodollar," Institutional Investor, International Edition, 6/82.

TABLE V

GROSS TRANSACTIONS IN AND NET PURCHASES OF FOREIGN STOCKS BY U.S. INVESTORS
($ Millions)

	1981		1982	
	Gross	Net	Gross	Net
Europe	$ 5,710	$316	$ 6,507	$ 773
France	823	69	785	203
Netherlands	251	39	427	99
Switzerland	933	33	707	75
United Kingdom	2,908	(38)	3,609	219
Canada	4,885	(583)	2,914	(72)
Asia	6,557	243	5,055	495
Japan	5,398	252	4,274	488
Other	1,598	212	1,041	101
All Countries	$18,750	$188	$15,517	$1,297

Source: U.S. Treasury

Net purchases of European stocks in 1982 increased to $773 million from $316 million in 1981, based mainly on net purchases of French and U.K. stocks in the fourth quarter. U.S. investors made net purchases of $203 million of French stocks, compared with $69 million in 1981. It seems incongruous that U.S. investors would be purchasing the stocks of French companies, given the steep deterioration of the franc over the year and the general lack of confidence in the economic policies of the French government. However, in the latter part of the year, the French government announced a new policy aimed at substantial injections of government funds into sectors ranging from footwear to machine tools in a bid to modernize production techniques and fend off competition.6/ With the French government expected to take a lenient stand towards foreign investment, the prospects of government aid and a somewhat steadier franc in the fourth

6/ "Europe," Financial Times Survey, 12/31/82.

TABLE VI

NET PURCHASES OF FOREIGN STOCKS
BY U.S. INVESTORS
($ Millions)

	1982 First Quarter	1982 Second Quarter	1982 Third Quarter	1982 Fourth Quarter
Europe	$ (47)	$ 55	$129	$ 636
France	(16)	(6)	51	174
Netherlands	(7)	19	13	74
Switzerland	23	26	14	12
United Kingdom	(64)	(10)	(4)	297
Canada	(162)	34	(66)	122
Asia	43	2	(12)	462
Japan	(34)	(9)	21	510
Other	(65)	8	58	100
All Countries	$(231)	$ 99	$109	$1,320

Source: U.S. Treasury

quarter may have caused a spurt of U.S. investment. Equally puzzling has been interest in U.K. stocks. Investors purchased $297 million of U.K. stocks in the fourth quarter, after making sales of $78 million in the first three quarters. While fourth quarter investment may represent speculative undertakings, it should be noted that British stocks outperformed those of other major foreign countries in 1982. Based on currency and market performance, the British stock market was the only one to show a positive net return in 1982.7/

Although there was no change in direction in 1982, the magnitude of net selling of Canadian stocks has subsided substantially. U.S. investors sold almost $600 million of Canadian stocks in the wake of nationalization plans in 1981, in comparison to $72 million in 1982. The Canadian government has taken a more moderate approach to energy policy, given the havoc

7/ "More Chills than Thrills in the Foreign Markets," Business Week, 12/27/82.

created by its original announcement. In addition, the outlook for Canadian export industries has brightened somewhat. However, U.S. investors will no doubt continue to follow a cautious approach to Canadian stocks.

Japanese stocks also benefitted significantly from the fourth quarter interest of U.S. investors in foreign securities, with net purchases of $510 million made. In 1982, net purchases of Japanese securities amounted to $488 million, almost two times the 1981 level. The Japanese yen rebounded more than 14% in the last quarter of the year on the narrowing of interest rate differentials between the U.S. and Japan. Moreover, the Japanese economy, although in recession, has outperformed those of the other major industrial countries. Nevertheless, domestic demand growth is not expected to provide enough stimulus to spur a strong recovery, and export growth hinges on worlwide demand and the constant threat of further protectionist measures.

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NOTE

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FOREIGN ACTIVITY IN U.S. SECURITIES

"HIGHLIGHTS"

1. In the first quarter of 1983, the U.S. economic outlook was promising, the stock market took healthy strides, and the dollar advanced against most major currencies. Given these encouraging trends, foreign net purchases of U.S. equities escalated by 72% to $2.7 billion from $1.5 billion in the last quarter of 1982. The $2.7 billion was very close to the quarterly peak of $2.9 billion reached in the second quarter of 1981.

2. European net purchases of $2.4 billion set a record quarterly high for that region. While investors from all major European countries were net purchasers of equities, purchases by U.K., Swiss and German investors hit record quarterly levels. U.K. investors purchased an exceptional $1.2 billion of U.S. equities, Swiss investors $536 million, and German investors $447 million.

3. As interest rates declined and the stock market rose, foreign investors clearly shifted their attention to equity rather than corporate bond investment. Foreign investors made net sales of $39 million of U.S. corporate bonds in the first quarter of 1983 and $176 million in the fourth quarter of 1982. In comparison, foreigners purchased about $1.6 billion of corporate bonds during the first nine months of 1982.

4. Foreign enthusiasm for U.S. Treasuries in the first quarter of 1983 remained on par with the 1982 level. At $4.1 billion, foreigners upped their holdings of Treasuries by 5% to $87.7 billion from $83.5 billion at year-end 1982.

5. In the fourth quarter of 1982, stock markets worldwide started to recover and declining U.S. interest rates omened a weaker dollar. U.S. investors made net purchases of $1.3 billion of foreign stocks. This revived interest in foreign stocks carried through the first quarter of 1983, although a more cautious approach was evident. Net purchases of foreign stocks by U.S. investors fell 25% to $994 million. While signs of global economic recovery are distinct and foreign stock markets recorded significant gains in recent months, the dollar's strength has overshadowed these factors.

Introduction

The 1982 level of foreign investment in U.S. equities supported the theory that no single factor is responsible for the decision to invest. While the dollar enjoyed a year of almost constant appreciation against most major currencies, monetary and fiscal policies were at odds as to how to stimulate a weak economy and the stock market languished through the first seven months of the year. Thus, foreign investment in U.S. equities receded 33% to $3.9 billion in 1982 from 1981's record $5.8 billion. However, in the first quarter of 1983, the U.S. recovery looked promising, the stock market advance continued, and the dollar remained strong. Given these trends, foreign investors boosted net purchases of U.S. equities to $2.7 billion from $1.5 billion in the last quarter of 1982.

Despite a downward revision in preliminary real GNP to a 2.5% annual rate, the general consensus remains that the U.S. recovery is well underway. However, the first quarter was punctuated with occasional fears of credit tightening by the Federal Reserve, given spurts of rapid monetary growth. While some interest rates did inch up in March after declining in January and February, the prime rate was lowered from year-end by 1 percentage point to 10.5% at the end of March. At the same time, the stock market took little note of rate fears and reached record levels during the quarter.

Positive signs of economic recovery are also emerging for many foreign countries. Nevertheless, it is expected that the recovery in the U.S. will be distinctly stronger than that in foreign countries. Moreover, the level of U.S. interest rates which has buoyed the dollar is still seen by many foreign leaders as hampering international recovery.

From year-end 1982 to the end of March 1983, the dollar scored moderate gains against most major currencies. Particularly sharp dollar appreciation was made against the British pound, 8.4%, and the French franc, 7.4%. The other major currencies gave up between 2% to 4% as the dollar advanced. Only the Canadian dollar held firm, remaining virtually unchanged from year-end.

The stock market gained impressively over the first quarter of 1983, boosted by expectations of lower interest rates and economic recovery. Both the NYSE and S&P 500 indices rose by almost 9%, while the DJI Average increased 8.0%. The robust stock market was probably the key attraction for foreign investors. The U.S. stock market has not been the only one to rally in recent months. However, in dollar terms, no overseas exchange performed as well as in the U.S., where signals of resurgence are strongest.*

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* "International Report," The New York Times, 4/4/83

Foreign Activity in U.S. Equities

Gross Activity

At $32.7 billion, first-quarter gross activity represents a 63% increase over the 1982 average quarterly pace of $20.0 billion. Much of the heightened activity level stems from Europe, with $19.6 billion of gross transactions reported for the first quarter of 1983. On a quarterly basis, regional activity patterns varied minimally. While gross purchases and sales originating in Europe were virtually unchanged, Latin American countries upped gross transactions by 7% to $3.2 billion. However, Canadian and Asian investors cut back activity by 8% and 4%, respectively.

Net Purchases

Foreign investors were slow to catch the market turnaround in late 1982. However, they were enthusiastic purchasers in the first quarter of 1983. At $2.7 billion, first-quarter net purchases of U.S. equities jumped some 72% from the fourth-quarter 1982 level of $1.5 billion and were just a shade below the quarterly record high of $2.9 billion reached in the second quarter of 1981. Large net purchases of $2.4 billion by European investors accounted for the bulk of the first quarter activity. Asian investors were the only ones not to share an enthusiasm for U.S. equities in the first quarter. These investors swung to net sellers of $306 million from net purchasers of $102 million in the previous quarter. In addition, although still net purchasers, Latin American investors reduced purchases by 76% to $56 million.

European Investors

In the first quarter of 1983, European net purchases of $2.4 billion of U.S. equities set a record quarterly high for that region. While investors from all major European countries were net purchasers, purchases by U.K., Swiss, and German investors hit record quarterly levels. U.K. investors purchased an exceptional $1.2 billion of U.S. equities, Swiss investors $535 million, and German investors $447 million. Investors from the Belgium-Luxembourg countries and the Netherlands swung from net sellers to net purchasers of $51 million each of U.S. equities. In addition, French investors escalated net purchases to $107 million.

TABLE I

GROSS TRANSACTIONS IN AND NET PURCHASES
OF U.S. EQUITIES
($ Millions)

	1982 Fourth Quarter		1983 First Quarter	
	Gross	Net	Gross	Net
Europe	$19,766	$ 860	$19,638	$2,444
Belgium-Luxembourg	687	(45)	619	51
France	2,064	4	2,023	107
Germany	1,559	211	1,815	447
Netherlands	843	(101)	821	51
Switzerland	6,503	(101)	6,358	536
United Kingdom	7,392	938	7,150	1,194
Canada	3,789	231	3,480	298
Latin America	2,973	235	3,192	56
Bermuda	1,078	68	1,154	72
Netherlands Antilles	769	99	901	(65)
Asia	6,260	102	6,006	(306)
Hong Kong	723	7	659	115
Japan	940	256	920	(186)
"Other Asia"*	4,343	(241)	4,000	(123)
Total All Countries	$33,119	$1,543	$32,726	$2,650

Source: U.S. Treasury

* Countries included are: Bahrain, Iran, Iraq, Kuwait, Oman, Saudi Arabia, the United Arab Emirates.

With general elections looming and the lure of a strong U.S. equities market, British net purchases jumped 27% to $1.2 billion in the first quarter from $938 million in the last quarter of 1982. The British pound fell precipitously over the first quarter, touching record lows against both the dollar and German mark. The uncertainty over the prematurely called general elections contributed to the pound's decline. However, Margaret Thatcher scored high in pre-election polls. Just as Thatcher's conservative government took much of the blame for the severity of the recession, it now can claim success for the budding recovery. Britain's deficit has been tamed to the lowest of all Western economies as measured as a percent of GNP, inflation is

at a 15-year low, and productivity has improved sharply.* Nevertheless, a weak international competitive position leaves serious obstacles to be overcome before Britain's high unemployment rate can be reduced.

Although cool to investment in U.S. equities in recent years, Swiss investors purchased $536 million in the first quarter of 1983. In contrast, Swiss investors made net sales in every quarter of 1982, cumulating in net sales of $524 million for the year. The Swiss franc declined a moderate 3.7% against the dollar in the first quarter. Despite this decline, the outlook for the Swiss economy remains cloudy. Some of the uncertainty stems from the course of the Swiss franc which, similar to the U.S. dollar, often serves as a "safe haven" currency in times of international problems. Upward pressure on the franc could jeopardize exports, thus choking off the recovery.

German investors have shown an unprecedented enthusiasm for U.S. securities recently, with $447 million of U.S. equities purchased in the first quarter of 1983. First-quarter net purchases are more than 2 times the fourth-quarter level of $211 million. Of the European countries, Germany is expected to lead in the recovery. However, real GNP for West Germany increased at a meager 0.5% annual rate in the first quarter and the mark wavered as the dollar gained. Both interest rate differentials and geopolitical events have undermined the mark's position and continue to spark capital flight.**

Canadian Investors

Net purchasers of only $226 million of U.S. equities in 1982, Canadian investors are maintaining the interest in U.S. equities that emerged in the last half of that year. Net purchases were boosted almost 30% in the first quarter of 1983 to $298 million from $231 million in the last quarter of 1982. With the decline of exceptionally high domestic interest rates, Canadian investors may have refocused their attention on equity investment. The Toronto Stock Exchange index recorded healthy gains over the first quarter, but not without frequent setbacks. The somewhat steadier rise of the U.S. stock market may have prompted increased Canadian investment.

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* "A Turning Point for the New Realism," Business Week, 6/6/83

** "Foreign Exchange Market Trends," Irving Trust Company, 4/21/83

Asian Investors

Investors from the Asian countries were the only ones whose activity in the first quarter resulted in net sales for that region. Net sales of $306 million of U.S. equities were made in the first quarter of 1983, representing a sharp swing from net purchases of $102 million in the fourth quarter. Mainly responsible for the turnabout was the swing by Japanese investors to net sellers of $186 million from net purchasers of $256 million in the last quarter of 1982. However, Japanese investors had made net divestitures of U.S. stocks through the first three quarters of 1982. With prospects for domestic companies picking up in light of the U.S. recovery, Japanese investors may be focusing on home markets. On the other hand, Mid-East investors were net sellers of U.S. equities in the fourth quarter and followed this pattern in the first quarter. Net sales of $123 million were made, compared with $241 million in the last quarter of 1982.

Foreign Activity in U.S. Corporate Bonds

As interest rates declined and the stock market rose, foreign investors shifted their attention to equities rather than fixed income instruments. Foreign investors made net sales of $39 million of corporate bonds in the first quarter of 1983 and $176 million in the fourth quarter of 1982. In comparison, foreign investors purchased about $1.6 billion of U.S. corporate bonds in the first nine months of 1982.

European investors swung to net sellers of $16 million of corporate bonds in the first quarter from net purchasers of $277 million in the last quarter of 1982. The ebbing enthusiasm of German investors accounted for this swing. German net purchases of $276 million in the fourth quarter were cut back to $37 million in the first quarter. The exceptionally large net purchases of German investors, $1.9 billion, in 1982 was prompted not only by interest rate differentials but also by the "safe haven" concept. Although German investment in corporate bonds was reduced substantially in the first quarter, net purchases of U.S. equities by these investors shot to a quarterly high. On the other hand, U.K. and Mid-East investors continued the net selling pattern established in 1982, albeit not at the same magnitude as in the fourth quarter. U.K. investors sold $100 million in corporate bonds compared with $185 million in the fourth quarter, while the oil-exporting countries sold $176 million compared with $292 million in the last quarter of 1982.

TABLE II

GROSS ACTIVITY AND NET PURCHASES OF U.S. CORPORATE BONDS
($ Millions)

	1982 Fourth Quarter		1983 First Quarter	
	Gross	Net Purchases	Gross	Net Purchases
Europe	$5,021	$ 277	$3,567	$(16)
Belgium-Luxembourg	126	(48)	70	(10)
Germany	1,524	276	1,089	37
Switzerland	534	68	454	68
United Kingdom	2,117	(185)	1,466	(100)
"Other Asia"	1,004	(292)	588	(176)
Total	$7,456	$(176)	$5,141	$(39)

Source: U.S. Treasury

Foreign Activity in U.S. Treasury Notes and Bonds

The average 1982 quarterly pace of foreign acquisitions of U.S. Treasury notes and bonds was almost matched by first quarter 1983 activity. At $4.1 billion, foreigners upped their holdings of U.S. Treasuries by 5% to $87.7 billion from $83.5 billion at year-end 1982. Movements of central banks to steady currency fluctuations have been overshadowed in the recent past by the activity of individual and institutional investors. In addition, policy statements have indicated that intervention in foreign exchange markets is being kept moderate.

TABLE III

NET FOREIGN PURCHASES AND TOTAL FOREIGN HOLDINGS
OF U.S. TREASURY NOTES AND BONDS
($ Millions)

	1982 Full Year		1983 First Quarter	
	Net Purch.	Estimated Holdings*	Net Purch.	Estimated Holdings*
Europe	$ 7,609	$27,503	$3,533	$31,036
Switzerland	693	1,080	(43)	1,037
West Germany	5,326	13,564	2,709	16,273
United Kingdom	(160)	6,549	929	7,478
Asia	10,831	49,637	(426)	49,211
Japan	797	11,577	158	11,735
"Other Asia"	7,534	34,826	(625)	34,201
All Countries	$17,267	$83,528	$4,139	$87,667

Source: U.S. Treasury

* Treasury has discontinued publication of the estimated foreign holdings of marketable Treasury notes and bonds. Therefore, estimated holdings are based on SIA's summation of reported monthly flows.

Returns on government issues followed an uneven course over the first quarter, with rates inching up to 10.85% by the end of March from 10.61% at the end of December. Attractive returns plus the traditional riskless nature of Treasuries kept foreign interest in these issues at a substantial level. German investors made net purchases of $2.7 billion, while U.K. investors made net purchases of $929 million. In contrast, based on large sales of $625 million by the oil-exporting countries, Asian activity resulted in net sales of $426 million.

The oil-exporting countries clearly reduced the pace of investment in U.S. securities in 1982, given the uncertain oil-pricing situation and dwindling current-account surpluses. Nevertheless, it is somewhat unusual for quarterly net sales of Treasuries to be reflected in the activity of oil-exporting nations as these instruments are considered the favorite investment vehicle of Mid-East investors.

U.S. Activity in Foreign Stocks

The attraction of U.S. investors to foreign stocks was almost nil in 1981 and 1982. However, in the fourth quarter of 1982, when stock markets worldwide began to pick-up and declining U.S. interest rates omened a weaker dollar, U.S. investors made net purchases of $1.3 billion. This revived interest in foreign stocks carried through the first quarter of 1983, although a more cautious approach was evident. Net purchases of foreign stocks by U.S. investors fell 25% to $994 million from the previous quarter. While there are distinct signs of global economic recovery and foreign stock markets have recorded significant gains in recent months, the dollar's strength has overshadowed the other major currencies. Given the unexpected strength of the dollar despite declining interest rates, U.S. investors appear to have moderated foreign investment.

TABLE IV

GROSS ACTIVITY IN AND NET PURCHASES OF FOREIGN STOCKS BY U.S. INVESTORS
($ Millions)

	1982 Fourth Quarter		1983 First Quarter	
	Gross	Net Purchases	Gross	Net Purchases
Europe	$2,668	$ 636	$3,188	$568
France	342	174	334	150
Netherlands	214	74	263	63
Switzerland	294	12	389	13
United Kingdom	1,411	297	1,507	207
Canada	1,048	122	1,182	80
Asia	2,032	462	2,479	469
Japan	1,756	510	1,979	339
Other	382	100	665	(123)
All Countries	$6,130	$1,320	$7,514	$994

Source: U.S. Treasury

In the first quarter of 1983, U.S. investors made net purchases of $568 million of stocks of European companies, a decline of 11% from the fourth-quarter level of $636 million. As in the fourth quarter, net purchases were concentrated in the stocks of the U.K. and France. U.S. investors' net purchases of U.K. stocks dropped 30% in the first quarter to $207 million from

$297 million. The steep depreciation of the pound coupled with the uncertainty of a general election may have dampened U.S. interest in U.K. stocks. In addition, British stocks which enjoyed a sharp runup in 1982 are thought by some money managers to be overvalued. U.S. investors also cut back net purchases of French stocks by 14% to $150 million in the first quarter. The level of U.S. purchases of French stocks rests at least in part on the assumption that President Mitterrand's socialist experiment was running out of time and the Government would be forced to take drastic action to make French industry competitive again.* The French franc has been beleagured since the Socialist government took power almost two years ago.

Net purchases of Canadian stocks were $80 million after reaching $122 million in the last quarter of 1982. Canada's stubborn double-digit inflation rate has given way in light of the wage and price restraints imposed last autumn and the economy seems poised for recovery. As prospects for the U.S. recovery improve, so too do prospects for Canada's export industries. Moreover, the Canadian dollar, which was quite volatile in 1982, was steady over the first quarter. The increased interest in Canadian stocks, however, is no where near the resource-stock led investment of 1979-80.

Based on their primary export market, Japan is another country which would benefit from a strong U.S. recovery. U.S. investment in Japanese stocks, although down from the fourth quarter level of $510 million, is still quite substantial at $339 million in the first quarter. The Japanese government has kept interest rates firm to protect the yen, which depreciated a minimal 2% against the dollar over the first quarter. In addition, Japan's current account surplus has grown partly as a result of lower oil prices and their is some evidence that exports have already begun to emerge from a year long decline.**

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* "International Report," New York Times, 4/4/83

** "Japan Delays Discount Rate Cut," Financial Times, 5/83